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Public debt in Africa: too high? too inefficient? at least too expensive

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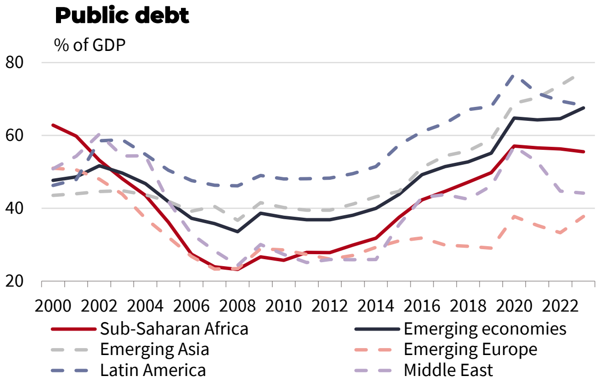
Since the early 2010s, Sub-Saharan Africa has seen a significant increase in its public debt. In addition, the proportion of public debt contracted "on market terms" is increasing. Unfortunately, these developments have not been accompanied by a significant increase in average levels of growth, public investment or infrastructure, while the capacity of the region's governments to raise taxes is showing little improvement. The combination of public debt becoming structurally less "sustainable" and a less favourable international environment for the region has led to increased refinancing risks. These risks could materialise in solvency crises and debt restructurings (this has already been the case for some countries in the region, such as Zambia and Ghana), events whose resolution remains complex despite attempts at better international coordination (such as the "Common Framework for Debt Treatments" of the G20 and the Paris Club).

Public debt has risen sharply, and its composition has changed

After a 2000-2010 decade marked by several sovereign debt cancellation initiatives (HIPC, MDRI, etc.[1]) – resulting in a significant fall in public debt levels in Sub-Saharan Africa (SSA) – the countries in the region have been in a new debt cycle since the early 2010s. The average level of public debt in the region (expressed as a % of GDP) is now comparable to the average level for emerging economies (chart 1)[2], and has returned to the level of the late 1990s, a period when public debt was less onerous (see below) and partially unpaid. Despite a wide range of situations, all the countries in the region have seen a significant increase in their public debt since 2010 (table 1).

[1] *Heavily Indebted Poor Countries Initiative, Multilateral Debt Relief Initiative.*
[2] *The "emerging economies" classification used here corresponds to the IMF's "emerging market and developing economies".*

Chart 1



Source: SG Economic and Sector Studies, IMF (World Economic Outlook)

Table 1

Public debt, % of GDP	2000	2010	2015	2020	2022
Average	63	26	38	57	56
Median	82	32	44	59	57
Min	8	8	14	17	15
Max	468	198	181	275	164
1st quartile	57	21	31	46	46
2nd quartile	82	32	44	59	57
3rd quartile	134	46	58	81	75

At the same time, the characteristics of this outstanding public debt have also changed:

- The countries of the region have gradually developed their local financial markets, which has made it possible to increase the share of domestic public debt (defined here as debt held by residents) to the detriment of external debt (held by non-residents). Domestic debt represented 44% of the region's total public debt at end-2021, compared to 22% in 2002 (chart 2). Even if there is little reliable/consolidated data giving a breakdown by creditors of this domestic public debt, the majority of this debt was made at "market conditions" (with local banks or on the local bond markets, therefore)[3].

- In connection with the greater integration of Sub-Saharan Africa into global trade and financial flows[4], the composition of external public debt has also changed significantly. Historical external creditors (multilateral[5], bilateral belonging to the "Paris Club"[6]) – which offer mainly concessional terms – have gradually given way to external commercial creditors (banks via international syndicated loans, international capital markets via bond issues – chart 3) with more onerous conditions, as well as Chinese creditors[7] with more "unclear" conditions. China is now the main bilateral creditor in the region (accounting for approximately 60% of its outstanding external public debt owed to bilateral creditors, compared to 3% in 2000[8]).

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[3] It should be borne in mind, however, that public indebtedness towards central banks is far from being eliminated, with some countries in the region making pronounced use of it (Nigeria, for example).
[4] This subject was discussed in greater detail in Risk&Opportunities n°2 and 3.
[5] World Bank, Regional Development Banks, etc.
[6] https://clubdeparis.org/
[7] Chinese state, Chinese state-owned banks, Chinese officially private banks.
[8] This corresponds to around 10% of total external public debt.

Chart 2

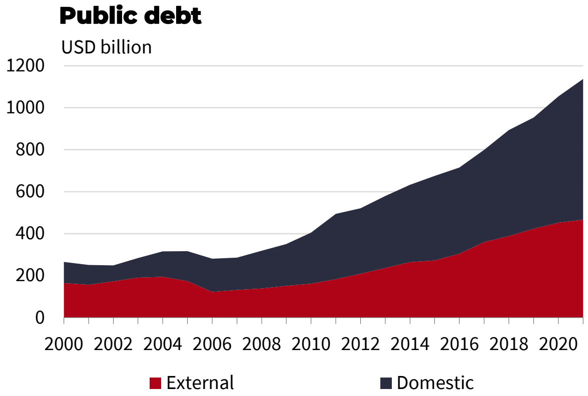
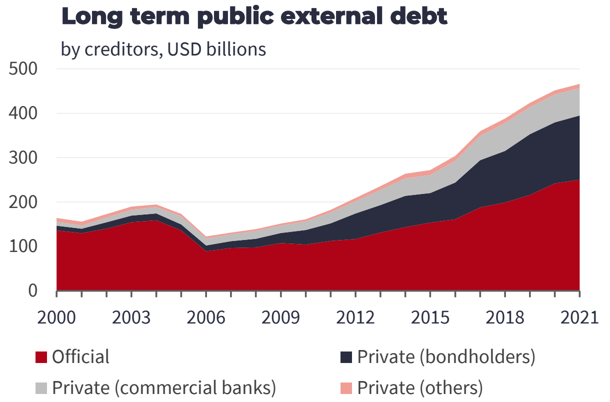


Chart 3



Source: SG Economic and Sector Studies, World Bank

All in all, an increasing proportion (since 2000) and today the majority of public debt in Sub-Saharan Africa is therefore on market – more expensive – terms. While the "cost" of domestic public debt is more difficult to comment on from a regional perspective[9], this increase is more evident in external public debt:

- Less than 20% of SSA's external public debt is now contracted on concessional terms (vs. a high point of 40% in 2005);
- More than 40% of it is now contracted at variable rates (vs. 17% in the early 2000s).

Potentially "inefficient" public debt, at least too expensive

The increase in public debt ratios across the region is not a problem as such. From a macroeconomic point of view, i) the vast investment needs identified in Sub-Saharan Africa over several decades[10], and ii) more generally the need to catch up with the wealth levels of more advanced economies, fully justify at least a temporary increase in public investment potentially financed by public debt. For its part, the increased use of so-called market financing (whether external or domestic") also reflects the region 's financial development[11].

Although the fragility of the region's statistical systems and the considerable heterogeneity of situations make any "regional" assessment difficult, it can

[9] *Because it depends mainly on macroeconomic developments country by country (inflation, tax revenues - see below).*
[10] *Physical infrastructure: roads, electricity, etc.; human infrastructure: education, health, etc. and even fighting climate change today.*
[11] *Meanwhile, several analysts/economists/politicians (regional or international), in favour of greater market and private sector participation in the development of Sub-Saharan Africa, argue that market-based financing, which is better priced than concessional financing, favours a better use of funds.*

nevertheless be seen that the sharp increase in public debt recorded over the past 15 years:

- Was not accompanied by a significant increase in average regional growth rates (chart 4).
- Was not accompanied by a significant increase in public investment (chart 5). In addition, it can also be noted that public spending in Sub-Saharan Africa remains concentrated on "current" spending: according to World Bank statistics, spending on public wages and subsidies/other transfers accounted for more than 60% of spending in 2020 (last year available), a figure that has remained broadly stable since 2012 (63%).
- Has not been accompanied, in all likelihood, by a significant "catch-up" in terms of infrastructure (physical or human), compared with other emerging or advanced economies.

Chart 4

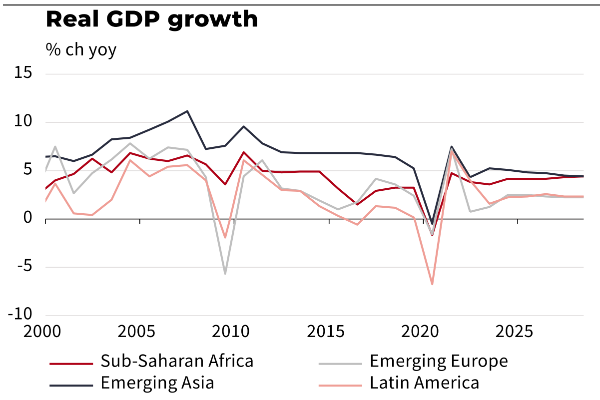
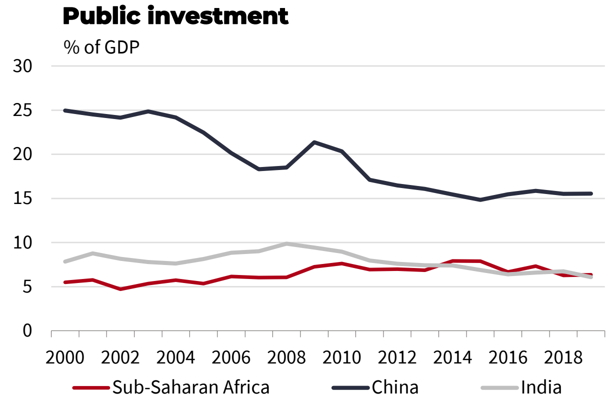


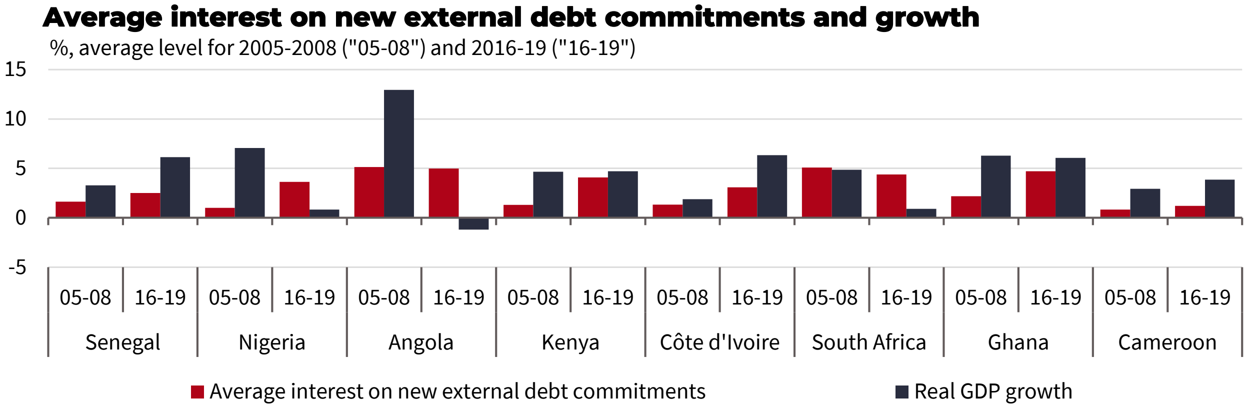
Chart 5



Source: SG Economic and Sector Studies, Refinitiv, IMF

Another way to illustrate the problem is to compare the change in interest rates at which "new" debt is contracted ("r") with real GDP growth ("g"). Reliable data on the interest rates at which "new" domestic public debt is contracted are difficult to obtain, but by focusing on external public debt (all creditors combined), this "r-g" analysis has evolved unfavourably for many countries in the region over the past 20 years (chart 6): the "g" factor has only rarely improved, while the "r" factor has deteriorated almost everywhere.

Chart 6



Source: SG Economic and Sector Studies, IMF, World Bank

In addition to not having the expected "knock-on effects", the increase in public debt has also made on terms that are too expensive, at least when compared to the region's budget revenues. Indeed, the rise in debt costs has not been accompanied by a parallel improvement in tax collection. This last point can be explained for a variety of reasons, but two structural factors appear to particularly hinder the ability of the states in the region to raise taxes:

- Levels of "economic informality" that are still significantly higher than those in other major emerging regions, and are only slowly declining (chart 7).
- Levels of governance (both economic and political) that do not show signs of "catching up" with the rest of the world (chart 8). However, this does not mean that governance has not improved in Sub-Saharan Africa over the past 20 years, but only that, on average, it has not improved faster than elsewhere.

As a result, tax administrations in the region are generally still too underdeveloped and have too fragmented a view of their economy[12] to be able to tax the wealth created properly.

[12] *This fragmented view is also linked to local statistical systems that are still deficient, as illustrated, for example, by the World Bank's "Statistical Performance Index" (https://www.worldbank.org/en/programs/statistical-performance-indicators)*

Chart 7

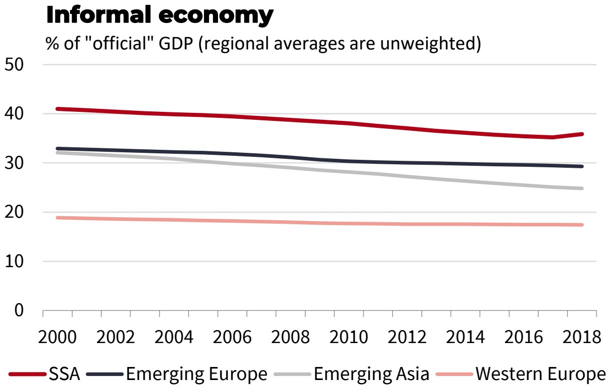
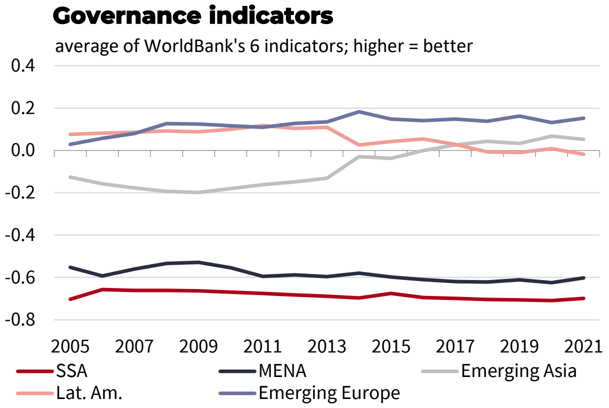


Chart 8



Source: SG Economic and Sector Studies, World Bank, Elgin, C., M. A. Kose, F. Ohnsorge, and S. Yu. 2021. "Understanding Informality", C.E.P.R. Discussion Paper 16497. SSA = Sub-Saharan Africa; MENA = Middle East North Africa

Overall, compared to the average of emerging economies, Sub-Saharan Africa has broadly similar public debt ratios (as noted above) but significantly lower budget revenues (chart 9). As a result, the "interest paid / budget revenue" ratio (perhaps the most important – in a 1st order analysis – when analysing the sustainability of public debt) has deteriorated sharply in Sub-Saharan Africa for about 15 years, with a dynamic that is now clearly diverging from that of emerging economies (chart 10).

Chart 9

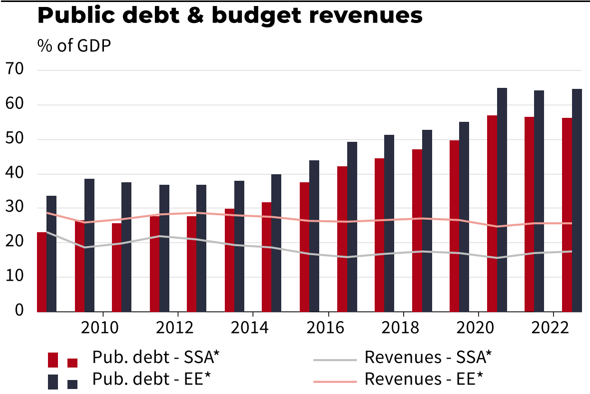
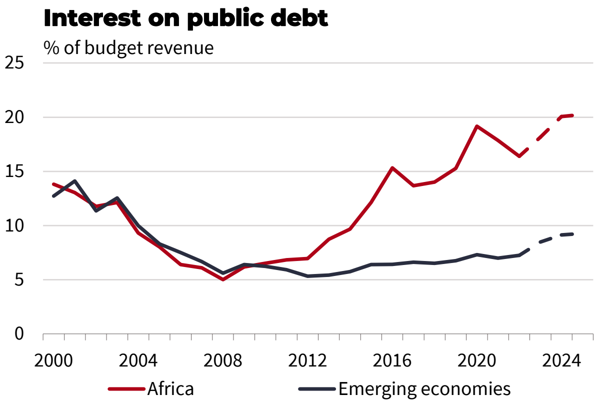


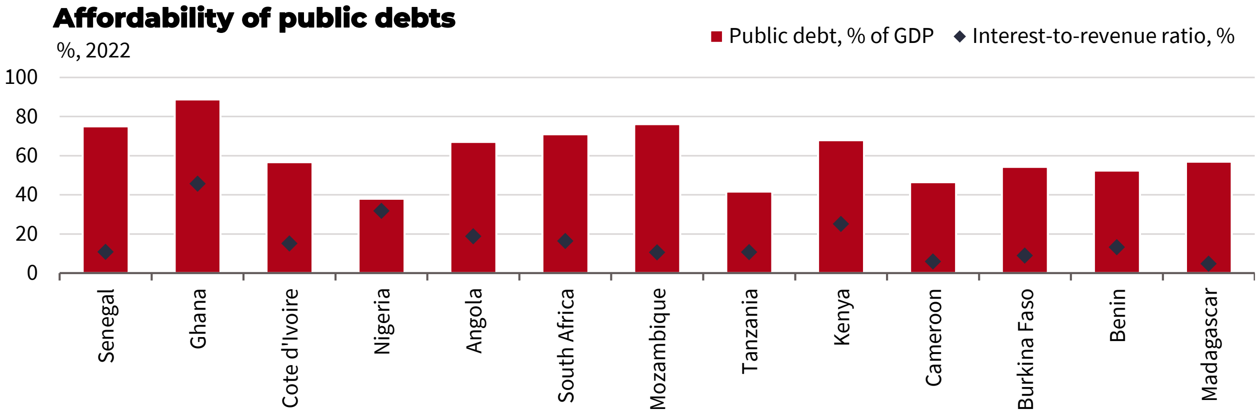
Chart 10



*Source: SG Economic and Sector Studies, IMF. *: SSA = Sub-Saharan Africa, and EE = Emerging Economies*

On this topic (as for most macroeconomic indicators in the region), there is considerable heterogeneity between the different individual situations (chart 11). Some countries have limited public debt but very high debt burdens, such as Nigeria. In line with what has been said previously regarding the diversification of sources of financing, the countries with the most fragilities (on this "interest / revenue" metric) are often "intermediate" or "advanced" countries of the region, having actually had access / recourse to private creditors (domestic or external) to get into debt during the last decade. By contrast, the "small", least developed countries (with, for example, lower levels of GDP per capita or economic structures still highly dependent on agriculture, etc.) did not have the opportunity to diversify their creditors, and therefore had to "settle" for their "historic" (i.e. official) one, on more affordable concessional terms.

Chart 11



Source: SG Economic and Sector Studies, IMF

Structurally less sustainable debt + more difficult economic environment = increased refinancing risks

This "scissors effect" between the increase in the cost of public debt on the one hand and the stagnation of budget revenues (expressed as a % of GDP) on the other hand, thus seems to be the main indicator of a less "sustainable" public debt overall in Sub-Saharan Africa. This deterioration is illustrated, for example, by the regular IMF/World Bank public debt sustainability analyses (DSA) of low-income countries[13] (chart 12). Of the forty or so countries analysed, no country in SSA currently has a "low risk of debt distress", compared to 13 countries in 2014.

This deterioration has – unsurprisingly – accelerated with the two consecutive exogenous shocks that have hit Sub-Saharan Africa since 2020, with the Covid crisis first and then the Ukrainian crisis from 2022:

- As in the rest of the world, these two shocks weighed on public finances in the region, both in terms of spending (in particular by maintaining current spending, which should have been reduced before 2020 – see above) and revenue (in particular in 2020, as a result of the 1st economic recession experienced by the region since 1992).

[13] *Low-income countries are the "IDA" and "Blend" countries of the World Bank: https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups*

- Moreover, while around 40% of regional public debt is denominated in foreign currency, the depreciation of local currencies (already recorded before 2020[14], and reinforced by the two exogenous shocks already mentioned) has automatically increased the weight of this debt (particularly in the face of a GDP always expressed in local currency).

Chart 12

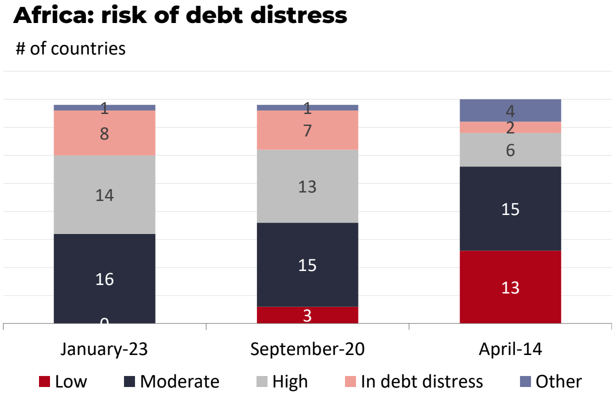
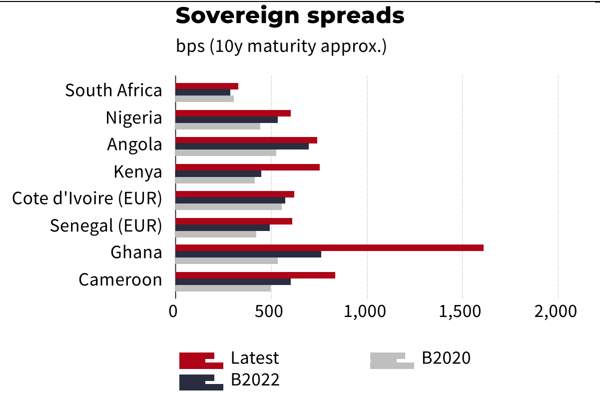


Chart 13



Source: SG Economic and Sector Studies, IMF, World Bank, Refinitiv

Finally, the start of Russia's invasion of Ukraine has also triggered a significant tightening of financing conditions for SSA countries, both in foreign currency and local currency:

- On the currency side, the combined increase in i) interest rates in advanced economies and ii) risk aversion has significantly reduced private creditors' appetite for Sub-Saharan African debt (as illustrated by high levels of sovereign spreads – chart 13). Countries in the region, which issued nearly USD 20 billion of international sovereign bonds ("Eurobonds") in 2018 [15], have lost access to international capital markets since April 2022. Syndicated loans to the region have also virtually disappeared (although reliable data on syndicated loans are more difficult to obtain). This is all the more problematic given that private creditors were the main financing source in the region between 2010 and 2019 (except in 2015 – chart 14). At the same time, while multilateral institutions have generally played their "countercyclical" role and increased their outstanding amounts on the region, net flows of external public debt[16] granted by bilateral creditors have been declining since 2014[17].

[14] *This is partly due to the region's structural current account deficit.*
[15] *And nearly USD 6 billion in 2020, the year of the Covid crisis.*
[16] *Net debt flows in year N represent the difference between newly disbursed debts in year N and capital repayments of existing debts in year N.*
[17] *Mainly due to a decrease in disbursements of loans ("new debt") granted by China from 2016 onwards, while official development assistance granted by Western countries was broadly maintained.*

- On the local currency side, the appetite of local financial systems – already greatly solicited over the past 15 years to cover public deficits – also seems to reach a 1st limit[18]. Over the past few quarters, most Sub-Saharan African states have been facing increasing pressure on their local financing conditions, through an increase in debt costs (yields required on new issues in local currency) or even increasing difficulties in covering all their financing needs.

This new "funding gap" (as described recently by the IMF[19]) automatically increases the zone's refinancing risks. While it is difficult to have a precise idea of the repayment schedules in local currency, external public debt amortization amounts due (capital repayments) to private creditors are more worrying. For example, Sub-Saharan Africa will have to repay USD 7 billion, then USD 9 billion in 2024 and then 2025 to its bondholders (chart 15), traditionally considered the most "demanding" creditors (see below).

A potential new "wave" of sovereign defaults in the region would likely have little impact on the rest of the world's economies and markets, especially given Sub-Saharan Africa's still limited weight i) in global GDP (just 2%), or ii) in global "financial assets". However, it would inevitably weigh on regional growth (at least temporarily), even though it is already insufficient to ensure real sustainable development in the region, given that population growth remains strong (+2.5% per year on average).

Chart 14

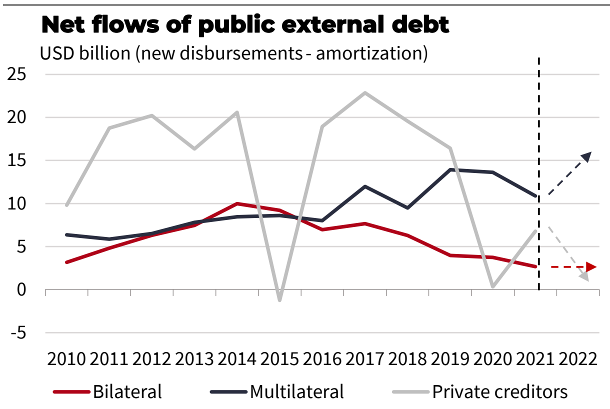
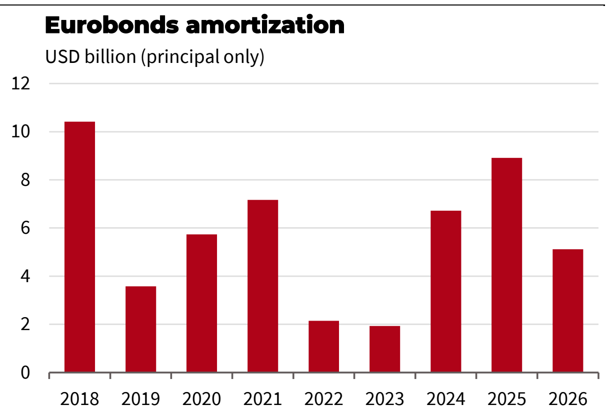


Chart 15



Source: SG Economic and Sector Studies, World Bank, Refinitiv

A liquidity problem (partially addressed through the DSSI) …

[18] *On average in Sub-Saharan African countries, outstanding local government debt accounted for nearly 20% of bank balance sheets before the Covid crisis. It is likely that this level has risen further since then.*

[19] *https://www.imf.org/fr/Publications/REO/SSA/Issues/2023/04/14/regional-economic-outlook-for-sub-saharan-africa-april-2023*

Faced with this double (structural and cyclical) weakening of their public finances, the countries of the region have already warned the "international community" in 2020 of the growing impossibility of matching the upcoming public debt refinancing obligations with the need to continue to "finance" growth (or even to accelerate it, see above).

As is often the case when the sustainability of public debts is called into question, a diagnosis of a "liquidity crisis" was made in the first place[20]. Thus, from the start of the Covid crisis, the G20 and the Paris Club (in April 2020) granted the "poor countries"[21] (most of them in Sub-Saharan Africa) a moratorium on the service of their public debt in foreign currency (interest and capital) due between May 1 and December 31, 2020. This moratorium – called the Debt Service Suspension Initiative (DSSI) – was then extended until the end of 2021. The DSSI will have had some success:

- 48 poor countries (out of 73 eligible), of which 32 in the region, benefited from it[22].
- Almost USD 13 billion in debt service was saved in total, of which probably around USD 6 billion for Sub-Saharan African countries.
- This initiative enabled – for the first time – China to be formally included in such an initiative.

However, while private creditors were (since the inception of the DSSI) invited to participate in this initiative "on comparable terms and on a voluntary basis" when debtor countries so wished, their involvement in the DSSI was non-existent, facing several difficulties:

- On the structural side, the absence of an international legal framework that could organize (or even compel in the most difficult cases) the participation of private creditors in a "review" of established debt agreements remains a major obstacle. The diversity of the interests and governance structures of the private creditors involved makes it difficult to coordinate their involvement (even when this seems desirable). In practice, private-sector involvement has so far been most common after a long period of accumulating sovereign debt payment arrears. Multilateral institutions usually want to avoid this default phase (whenever possible) and push negotiations as soon as they are needed

[20] Broadly speaking, a debt crisis can be diagnosed in two ways: a situation of illiquidity, where the debtor experiences a temporary cash flow difficulty but can pay in the future, provided he is given time; and a situation of insolvency, where repayment is not possible either at present or in the future.

[21] The World Bank's IDA category, and the United Nations' Least Developed Countries.

[22] The only eligible countries in Sub-Saharan Africa that have not participated in the DSSI are: Benin, Ghana, Nigeria, Rwanda, Somalia and South Sudan.

for debt sustainability assessments; but they lack the means to force such negotiations on private actors.

- On a more cyclical level, from the outset of the DSSI, credit rating agencies have communicated that any debt write-off involving private creditors[23] – even if voluntary – would result in putting the securities concerned in default. Countries in the region then feared long-term loss of access to international financial markets, and overall, have taken very few steps to include their private creditors in any moratorium.

… to a solvency problem (the possible resolution of which remains more complex)

Despite its success, this temporary initiative has focused on countries' (potential) liquidity problems, without addressing the more structural deterioration in Sub-Saharan Africa's debt solvency (described above). In response, in November 2020, the G20 and the Paris Club developed a "Common Framework for Debt Treatments" (CFDT), "to facilitate timely and orderly debt treatment for DSSI-eligible countries, with broad creditors' participation including the private sector"[24]. The CFDT is based in particular on three structuring principles:

- The need for a prior diagnosis of insolvency, based on the debt sustainability analysis conducted jointly by the IMF and the World Bank (see above). The two institutions thus continue to play a key role in debt restructuring processes, as their analysis also makes it possible to "frame the discussion" on the perimeter of the debt to be restructured (including domestic public debt or not, etc.) as well as on the levels of effort that will subsequently have to be made by the debtor country and its various creditors (even though these analysis are sometimes perceived as not very transparent by private creditors).
- Coordination among official bilateral creditors, which "formalizes" China's inclusion in such discussions.
- Comparability of treatment with other creditors, which also confirms that when bilateral creditors grant debt relief, an equivalent private sector involvement is expected. Specifically, a country requesting debt restructuring "will be required to seek from all its […] private creditors[25] a treatment at least as favourable as the one agreed" with its official creditors.

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[23] *Rating agencies usually exclude from their methodology the "treatment" of debts owed to official creditors.*
[24] *https://clubdeparis.org/sites/default/files/annex_common_framework_for_debt_treatments_beyond_the_dssi.pdf*
[25] *As well as from any other bilateral creditors outside the G20 and Paris Club.*

Soon, several countries in the region applied to restructure their external public debt under this framework: Ethiopia, Chad, Zambia, and Ghana. Although it is still far too early to draw a definitive assessment of the CFDT, it seems that it does not – for the time being – represent a significant simplification of a restructuring process that remains long, complex and creates tensions between creditors and debtors on the one hand, and among creditors on the other. To date, only Chad and Zambia have reached certain “milestones" of the CFDT:

- Chad: after opening negotiations (without defaulting) for a possible restructuring in early 2021, progress was initially slow. Then, higher oil prices in 2022 reduced the urgency of finding a solution, and creditors concluded in October 2022 that the country no longer needed debt relief. They pledged to meet again if a funding gap was identified. The country’s case was relatively “easy,” as Chad has no eurobond and its external commercial public debt is almost exclusively owed to a single creditor (an oil trader).
- Zambia: the country “joined” the CFDT in November 2020, having formally defaulted on its external bond debt and accumulated large arrears to its other creditors. Discussions with both private and official creditors have been difficult. For the latter, the preponderance of Chinese creditors (state, public banks, private banks)[26], unaccustomed to this type of “collective bargaining”, probably contributed to this difficulty. In June 2023, Zambia finally reached a restructuring agreement with its official creditors (with outstanding loans of around USD 6.3 billion). However, contrary to the spirit of the CFDT (see above), an agreement between Zambia and its private creditors remains to be found (for an outstanding amount of approximately USD 6.8 billion), and it is unlikely to be on terms comparable to those of the agreement with official creditors.

After restructuring part of its domestic public debt between December 2022 and February 2023, Ghana formally began discussions with its external creditors in May 2023. While an agreement with official creditors could be reached relatively quickly[27], an agreement with private creditors seems more distant. Finally, the case of Ethiopia is even more complex and with even less progress[28].

All in all, it seems for now that the diversification of the creditors affected by possible debt restructurings in Sub-Saharan Africa has complicated the process (by multiplying interlocutors and points of view), with the CFDT providing only limited “help”. Indeed, some progress has been made here, with the inclusion of “new bilateral creditors” (mainly Chinese), who were previously excluded from the Paris Club’s normal procedures. Indeed, negotiations with official creditors, which in the

[26] *Accounting for more than 25% of outstanding external public debt according to Moody’s.*
[27] *“Atypical” bilateral creditors such as China are less prominent in Ghana’s external public debt.*
[28] *Mainly due to the civil war that hit the country between end-2000 and end-2022 (with possible international repercussions to be determined).*

past had to be conducted in a "fragmented" manner (Paris Club bilateral– "Western" – and multilateral creditors on the one hand; other bilateral creditors on the other), can now take place in a single forum and in a more coordinated manner.

However, despite this real but limited progress, negotiations with official creditors, while often the first to be concluded, are still generally lengthy[29]. Moreover, the "voluntary" participation of private creditors remains very complex to coordinate in the absence of an international legal framework.

Still, it would be helpful for the region (and emerging countries more generally, because public debt solvency issues are not limited to Sub-Saharan Africa) if a smoother process could be found. Indeed, it will be essential for the countries concerned to be able to rapidly free up new investment capacities (whether public through budgetary expenditure, or private through a greater participation of private actors which would have been reassured in the macroeconomic prospects of the countries concerned), as the economic, social and, above all, climate-related challenges call for significant spending in these areas. As indicated in previous Risk&Opportunities (n°18 and 19), the climate investment needs for Sub-Saharan Africa are indeed considerable: in 2020, for example, the IMF estimated that adaptation costs alone could amount to USD 30 / 50 billion per year by 2030[30]. These amounts are also in addition to other necessary investments in equally priority sectors: "physical" infrastructure (energy, water supply and sanitation, information and communication technology, road transport and other transport infrastructure, etc.) or "human" infrastructure (health, education, poverty reduction, etc.).

[29] *And not necessarily shorter than in the past. The inclusion of "Chinese creditors" was not without problems, mainly due to i) a persistent lack of transparency on debts granted (amounts, conditions, or even classification of the lender as sovereign, public bank or private bank), and ii) positions that are sometimes "atypical" during negotiations. For example, when Zambia's debt was being restructured, China asked for multilateral and regional development institutions (IMF, World Bank, African Development Bank, etc.) to be included in the restructuring. This type of creditor is traditionally not involved in debt restructuring operations, in particular in order to preserve their ratings and, de facto, their ability to take on debt and then "re-lend" the funds raised to countries whose solvency is fragile.*

[30] *As stated in Rik&Opportunities n°18 and 19, the main challenge for Sub-Saharan Africa is not so much to mitigate (reduce) greenhouse gas emissions, but mainly to adapt as best as possible to the negative effects of climate change.*

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